RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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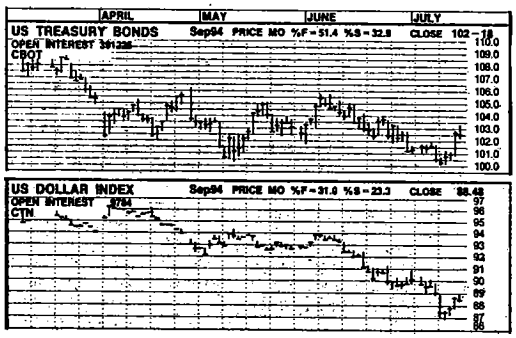
July 20, 1994 **LETTER 1152**

July 8 DJIA 3709.14; PTI 3993; A-D Ratio -6.78
July 15 DJIA 3753.81; PTI 3998; A-D Ratio -6.19
Dow Yield: 2.71%; Dow Price/Earnings: 25.7
Dow 200-day MA: 3749; Dow 30-day MA: 3726
Dow Times Book Value: 3.35; PTI 89-day MA: 4016
Percentage of Undervalued Blue-chips: 14%
Dow Low Risk Buy Index: -7; Gold-PTI: 937
Gold 40-week MA: 381

"HAVE A NICE DAY" ("nice day" charts courtesy of *Investor's Business Daily)*



BEAR MARKET? The "experts" continue to argue about whether this is a bear market or not. Many Wall Street analysts and brokerage letters insist that we're still in a bull market. I disagree, but I want to discuss the whole issue further.

How do you identify a primary bear market? First, authentic bear signals come only during or following the third (psychological) phase of a bull market. The third phase of a bull market is characterized by heavy volume, intense public participation, rampant speculation, high-flying new issues, and flagrant overvaluation in most stocks (the last can be identified by low dividend yields on the major averages).

There's no doubt in my mind that the early years of the 1990s marked the third phase of the great 1974-94 bull market. Therefore, I was ready to accept as authentic any Dow Theory bear signal that appeared within the context of the recent third phase.

Next question -- what constitutes a Dow Theory bear signal? This is what a bear signal looks like: the two D-J Averages, Industrials and Transports, rally to new highs. They then turn down for a period of three or four weeks or longer in what appears to be a secondary "correction." Following the correction, the Averages rally again. If, on this rally, both Averages break to new highs, the "all clear signal" will be given. However, if one or both Averages fail to advance to new highs and the two Averages then turn down, the situation becomes critical. For if, on the decline, BOTH Averages break the preceding "correction" lows, a bear market will be signaled. If volume expands dramatically on the breaking of the lows, the authority of the bear signal is enhanced.

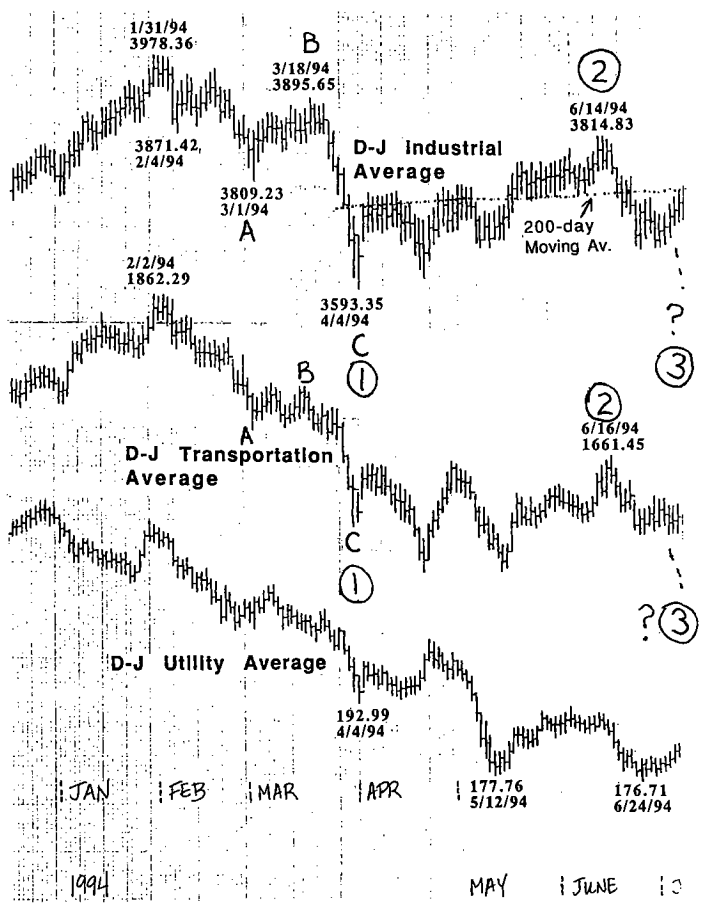
All right, please refer to the page 1 chart of the Averages. I called a bear market based on the A-B-C downward zig-zag pattern in the Dow Industrials and the extremely weak A-B-C pattern in the Transports. True, the A-B-C formations in both Averages were "small," and for that reason many Wall Street commentators disagreed with my bear market call. Their argument -- the decline to point A was not great enough in either duration or extent. In other words, the whole A-B-C pattern was too minor to be taken seriously as the signal for a primary bear market.

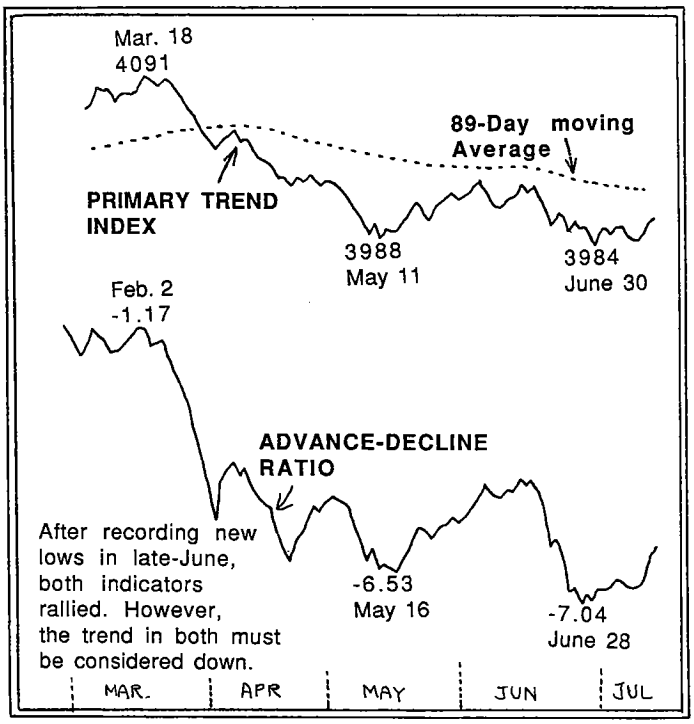
My response -- I felt that the A-B-C pattern, following almost three years of uncorrected market action, was sufficient. I also took into consideration the collapsing Utility Average. On top of that, I felt that the Transport action was so weak that it confirmed my belief that a bear market was signaled. I am still of that opinion -- a primary bear market definitely was signaled on March 27 under Dow Theory (by the way, the 1929 bear market signal was also attacked at the time as being "minor and too insignificant").

How about a re-test of the current market situation? How about a confirmation of my bearish call? Fair enough. If I am correct, if this is indeed a bear market, then this market (somewhere ahead and in its own good time) will head down again in earnest. Remember, and this is a very important concept -- in a bear market values erode through time. In other words, the longer the elapsed time, the greater the odds that stocks and the market will be heading down.

We now have very important downside levels. I am referring to the 1994 lows for the Averages at the points marked (page 1 chart) with the circled (1). We also have the subsequent rallies to the points marked with the circled (2). This makes for an interesting situation.

If somewhere ahead the Averages turn down and break below the April lows at (1), we will then have what every student will have to





admit is a very large (1)-(2)-(3) downward zig-zag or definitive bear market pattern. At that juncture, I don't think there will be any argument about whether this is a bear market or not.

But wait -- what if both Averages turn strong and advance to new record highs? If that happens I will admit that I was wrong and that the bull market continues in force. Even then, however, two factors would really bother me. (1) The advance-decline ratio (see page 2 chart) has been so battered and is still so weak that I personally would remain skeptical, and I would stay on the sidelines. (2) New highs in the Dow would mean that the Dow yield would remain dangerously low, and as far as I am concerned, the market would continue to be perched precariously on "thin ice."

In closing this section let me warn subscribers that if the April lows are jointly broken, I would expect to see a powerful, maybe even a panicky decline (since at that point the bear market would resume in full force, following its April to July "resting period").

THE DOLLAR: I guess what bothers me most about the recent dismal and bearish dollar action is that people haven't taken it seriously. The talk of the nation is about the O. J. Simpson trial, not about the ghastly hemorrhaging of the once "almighty dollar." But I take the bear market in the dollar very seriously.

Consider this. The dollar is a fiat currency. There's nothing intrinsic behind the dollar -- no gold, no silver, not even any copper or nickel. The only thing behind any fiat currency is confidence, and when a fiat currency heads down it always signifies a crisis of confidence in the government that stands behind that currency.

Let's face it, international capital doesn't like the Clinton administration, and it doesn't like the fact that US "prosperity" is being financed by foreigners who are taking in $14 billion additional dollars a month. Furthermore, the world knows that a negative current account balance of (annualized) $150 billion is unsustainable.

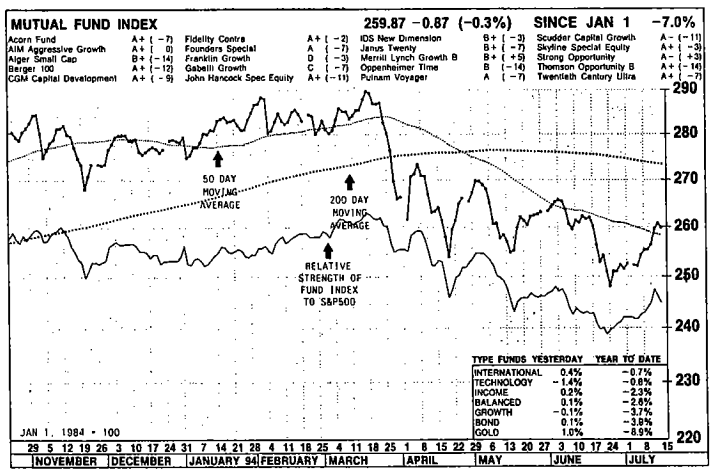
From a market standpoint, if the dollar continues to slump, at some point such action will force the Fed to move on interest rates -- or it will set off a panic of selling by foreigners, and I mean selling bonds, stocks and anything denominated in dollars. After all, there's a limit to how much of a beating our creditors can be willing to take.

Consider this: if you're a German or a Japanese investor (or central bank) you've taken a 10% to 15% beating on your long US bonds based on rising interest rates plus another 10% to 12% whipping based on the slumping dollar. Figure it out -- that's a crushing loss in bonds, to say nothing of any other holdings that you might have in the US.

The bear is sneaky. He's been attacking the nation in one area that Americans are least familiar with -- their currency. The dollar, the current account, the debt, it's all part of the slowly unfolding bear market picture. Rising debt and an increasing outflow of dollars are rapidly reaching the point of no return. And unfortunately, there's no painless solution to the problem. The bear knows this. But he's patient -- he's biding his time.

MORE MARKET: Subscribers ask me how best to gauge what the market is doing. Every analyst has his own answer to that one. Some follow the broad Wilshire 5000 Index, some like the blue-chip Dow, others say the Value Line Geometric, and still others prefer the S&P 500 or the NYSE Composite.

Me, I watch them all. But increasingly I keep my eye on still another gauge. The bulk of the public's "investment" money is now in mutual funds. For this reason, I believe that *Investor's Business Daily's* Mutual Fund Index provides us with a quite accurate picture of how the average person is doing in the market. In the last Letter I described the Mutual Fund Index in detail, and I include an updated chart of the Index below.


MUTUAL FUND INDEX
259.87 −0.87 (−0.3%)
SINCE JAN 1 −7.0%
50 DAY MOVING AVERAGE
200 DAY MOVING AVERAGE
RELATIVE STRENGTH OF FUND INDEX TO S&P500
TYPE FUNDS YESTERDAY YEAR TO DATE
INTERNATIONAL 0.4% −0.7%
TECHNOLOGY −1.4% −0.6%
INCOME 0.2% −2.3%
BALANCED 0.1% −2.6%
GROWTH −0.1% −3.7%
BOND 0.1% −3.8%
GOLD 1.0% −8.9%
JAN 1, 1984 = 100
NOVEMBER DECEMBER JANUARY 94 FEBRUARY MARCH APRIL MAY JUNE JULY

I just went over the record of the funds for 1994. Of the 50 largest equity funds, only four showed a positive total return for the first half of this year -- all the others showed losses, with many registering sizable losses -- such as 20th Century Ultra (down 10%), Fidelity Magellan (the largest of all the funds and down 6%) and Franklin Custom Utilities (down 16.5%). A number of funds with the hottest five-year records are now showing losses since their January 31 market peak. Examples: Berger 100 -- down 16.9%; Thompson Opportunity B -- down 22.8%; ABT Emerging Growth -- down 17%; Keystone S-4 -- down 18.2%; J. Hancock Spec. Eq. A -- down 18.3%.

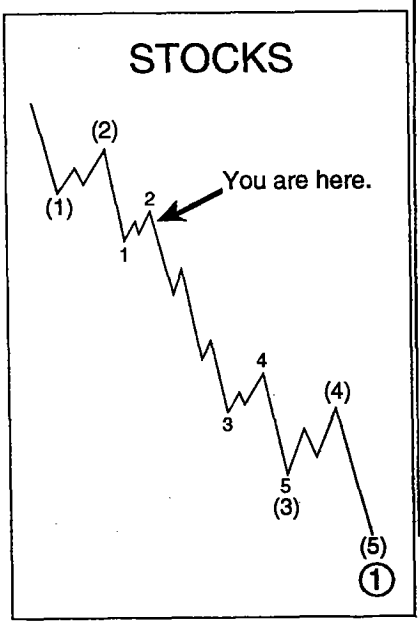
Subscribers might as well know my prediction for the mutual funds. Before this bear market is over I expect the entire mutual funds to be a disaster area. The funds will be as disliked at the final bear market lows as they were loved at the bull market's high.

Next, I want to provide a bit of long-term perspective. I take the bull market as having started in late-1974 and having ended in 1994. This makes it the longest bull market (in duration) and one of the largest (in extent) in stock market annals.

History tells us that whereas bull markets have no apparent relationship to the bear markets which preceded them, bear markets do have a relationship to the bull market which preceded them. Since we have just concluded a 20-year bull market which advanced the Dow from 577 to just under 4000, I now expect a bear market that will ultimately correct the entire 1974-1994 advance.

We are now in a primary bear market. This means that the tide has turned, and from a long-term perspective the market will be heading down -- down to where, finally, the Dow will provide a yield of 6% or better. Frankly, I don't know what path the Dow will choose to get to the 6% yield zone. Nor do I know how long it will take for the Dow to get down to the 6% zone. But I'm betting that somewhere ahead we will see a 6% or better yield on the Dow, and I'm betting that in coming years we will see a string of bearish events, events that will justify a yield of 6% (or even higher) on the Dow.

Bob Prechter writes *"The Elliott Wave Theorist,"* and unlike this writer, Bob does have an idea of just what type of pattern the averages will take as the bear market unfolds. You may or may not believe in the Elliott Wave thesis, but Prechter is a keen student of the market, I respect him, and I have followed his work for many years. At any rate, this is Bob's "blueprint" for the form the Dow will take as this bear market progresses. He also shows us where he believes the Dow is now.



Note that what Prechter pictures here is only the first declining wave of this bear market. What we see here is a complex wave composed of three down legs (1), (3) and (5) and two intervening rising or corrective legs, (2) and (4). But the entire wave pictured is simply the first down-wave in the bear market. According to Elliott, once this down-wave is completed, there will be a large corrective wave stretching from ① up to ② (not shown), and then a crushing downwave taking the market to a final bear market low at point ③ (which is also not shown). Prechter believes that the final downwave will take the Dow below 1000. Sounds crazy, doesn't it? But then, which of us back in 1974 with the Dow at 577 thought we'd ever in our lifetime see the Dow advance to just below 4000? (Chart courtesy of *Elliott Wave International,* Box 1618, Gainesville, GA 30503.)

Comments: 38% of all the stocks on the NYSE are now interest rate sensitive. Declining rates during the last three years were clearly a big plus for the stock market, and it showed particularly in rising market breadth (i.e., the advances and declines). But now the situation is reversed. With interest rates in a rising trend the pressure is on those same 38% of stocks (utilities, banks, insurance, small loans, brokers, etc.) and this is a decided negative for the daily advances and declines.

Damage: One-third of all stocks are now down 30% from their 52-week highs. One-quarter of all stocks are now down 40% from their 52-week highs . . . In his latest report Joe Granville counts 693 NYSE issues having declined within one point or less of their 52-week lows. You can almost sense this as day after day we count more new lows than highs on the NYSE. This is internal deterioration, and it's bearish.

INVESTMENT POSITION: I guess you could call this (so far) the "Stealth Bear Market" because the real damage is not that apparent on the surface. No, the real damage has come in the non-Dow stocks and in the interest-sensitive stocks. But the world watches the Dow, and there we have yet to see as much as a 10% correction on a closing basis.

Speaking of the Dow, some investors have done well (in the bull market, this is) by staying with the top five yielding Dow stocks, adjusting every six months or even once a year by switching to the new top yielders. So for the record, the top Dow yielders are now Woolworth (7.54%), Philip Morris (5.45%), Exxon (5.05%), JP Morgan (5.01%), Chevron (4.17%). If this was a bull market I'd buy all of them. But as this is a bear market, I'm just posting the above for the record.

Cash and gold items are my choice to weather this bear market. It all reminds me of an incident which occurred after the San Diego Chargers won a particularly tough game with the LA Raiders. Following the game a radio announcer interviewed the San Diego coach. "Wow, great game Coach, do you have any comments about your victory?" "Yeah, I do," replied the nervous San Diego coach, "we were just glad to get out of there alive."

I haven't forgotten the coach's words, and I think that his attitude might serve us well as this bear market progresses. Never mind "beating the bear." Never mind that your neighbor made a big profit in some weird little stock that his broker whispered to him. The idea now is not to lose money, or at least to hold losses to a minimum. In other words, don't get greedy, don't do anything crazy -- let's just think in terms of "getting out of this blasted bear market alive."

Note: Much publicity is now being given to the fact that insiders have stepped up their buying substantially in their own companies. Insiders may know their companies, but they don't know the market. Insider buying during a bull market makes a lot of sense. Insider buying during a bear market tends to produce less affluent insiders.

CHEAP DOLLAR: I've been pondering the cheap dollar for a long time. Consider this: (1) The US is the world's only remaining super-power. (2) The US economy is in an uptrend. (3) The dollar is the world's reserve currency. (4) US interest rates are in a rising trend (which should be bullish for the dollar).

In view of all the above, why is the dollar's purchasing power parity so low and sinking? In other words, why does the dollar buy so little in Japan or Italy or Germany or France or even in Britain? This whole question is one that no one seems to want to address. Certainly, nobody in Washington wants to tackle this basic question.

Why don't they? Why doesn't the President or the Treasury Secretary address the question of the dollar's lowly purchasing power in international markets? Answer: Probably because it would be too embarrassing. Too many facts would have to be brought out.

The answers to the cheap dollar, as I see it, are as follows: (1) The sinking dollar is an international judgment on the current administration and its policies. (2) The world is holding too many dollars. They're literally piling up. (3) The US current account balance is running at a negative rate of around $150 billion a year, meaning that huge quantities of "newly-manufactured" dollars are flowing out of the US to governments and businesses overseas. (4) The embarrassingly low savings rate in the US (3.5%) is a major negative for the dollar. (5) The chronic US deficits frighten foreign dollar holders. They know that a nation with chronically large deficits and a low savings rate will also have a weak currency. (6) The ever-climbing US national debt frightens dollar holders. They know that the federal debt (now approaching $5 trillion) will never be paid off. If it isn't paid off, how will it be handled? It will be handled by systematically reducing the value of the dollar. (7) It seems clear that the Clinton administration is allowing the dollar to seek its own level in the international market, a policy known as "benign neglect." (8) The world suspects that the Clintonites really want a lower dollar, particularly against the yen. This, supposedly, will force the Japanese to address our severely adverse trade deficit with Japan.

Most of the above, you argue, are long-term considerations. But why should those long-term considerations impact on the

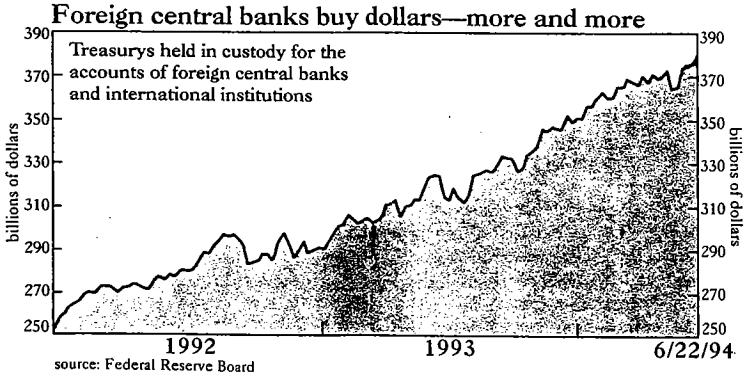
purchasing power of today's dollar? After all, the dollar still buys a lot of food or clothes or housing in the US. For example, it costs you $39 to buy a good cotton shirt in the US, but it costs you an outrageous $69 for a decent cotton shirt in London.

One answer to the dollar riddle is that overseas businessmen and investors tend to think in longer terms. In Europe, particularly, they are very aware of the damage that inflation can do. Furthermore, the key European currency, the D-mark, is a German issue, and the Germans (within this century) have had two absolutely disastrous bouts with inflation. Thus, the Germans, and evidently most of Europe, are extremely suspicious of a nation which has followed a policy of inflating its currency ever since World War II. Furthermore, recent remarks by high-placed Germans were actually contemptuous of US financial policies (the Germans stated that they did not want to waste any more money on useless intervention).

So the conclusion is that if you're a visitor to the US you can buy a lot with your francs or marks or yen. If you're an American tourist in Europe or Japan, your dollar won't buy you much. If you're an overseas investor, you don't want to hold dollars for too long. And if you're an American, unfortunately, you're probably oblivious to the big picture.

This is a chart courtesy of *Grant's Interest Rate Observer* (30 Wall St., NYC 10005). You think there's no problem in supporting the dollar? Wrong. The graph depicts the steady build-up in dollars which foreign central banks are faced with. As Grant says, "Unless this dollar buying is sterilized, it must eventually produce new central bank liquidity. And if it is sterilized, what good will it do? In the past 12 months, foreign central banks have increased their dollar holdings by **16.5%**. In the private sector, that's known as averaging down." Russell comment: In other words, supporting the dollar by foreign buying of dollars will produce overseas inflation. It will also produce problems for the central banks in that they will be loading up on an eroding asset, an asset that they have enough of already.

Foreign central banks buy dollars—more and more



source: Federal Reserve Board

BONDS: The real losses in this bear market, so far, have come in the interest-sensitive items, namely utilities and bonds. Remember this, the total debt of all kinds in the US adds up to $15.9 trillion (that's trillion). When interest rates rise (due to the weak dollar) the losses hit that $15.9 trillion in total debt. Thus, a 1% rise in interest rates wipes out tens of billions of dollars in total debt values, values stretching out to utilities, corporate, municipal and government bonds, bond funds, mortgage debt, etc.

I just don't think that most people realize the implications of rising interest rates in a nation with $15.9 trillion in debt. To put it mildly, the implications are staggering.

And it's a paradoxical dilemma. If the Fed wants to protect the dollar, they will have to raise rates. And if they follow a practice of benign neglect, the dollar continues to decline which impacts on bonds, and as bonds fall, rates rise. Either way, it seems, rates are fated to rise.

Further complicating the picture is that most of the world's economies are now expanding. This means that there is an urgent global need for capital. But the world money supply is in a declining trend. Thus the competition for capital also militates towards higher rates.

NOTES & QUOTES: What's constitutes an American patriot? Russell's answer -- a person who believes in and defends the Constitution of the United States. Few Americans have actually read the Constitution. Far fewer have studied it. And apparently not many politicians believe what it says.

A few weeks ago I was visited by subscriber David Stedman of North Carolina. Stedman is a true patriot; and he has through his trust published a marvelous book entitled, "Our Ageless Constitution." As I read this book I feel my blood boil, particularly regarding the section on the Federal Reserve, banking and the dollar. How certain men flagrantly subverted the Constitution, how the Federal Reserve was created as a quasi-private institution to create a fiat currency, how the dollar (originally defined in terms of specific quantities of silver or gold) was degraded and turned into a worthless piece of cotton and linen, how our coinage was debased and its silver content removed, the whole story is enough to make one raise a fist towards Washington and the cowardly politicians who have either fomented these outrages or allowed them to happen.

In order for democracy or a republic to survive, there must be an informed electorate. We don't have that. The politicians are active and the populace is passive. Unfortunately, America's voters only become active in the face of emergency or chaos.

I predict that somewhere in the future the dollar will collapse and there will be chaos. At that point the media will be forced to delve into why it happened and how it happened. Then the whole scandalous story of the Federal Reserve, the Sixteenth Amendment (the income tax) which was never legally ratified, the bastardization of our currency, the deficits, the whole sickening story of how the Constitution was subverted, all of this will be made public and I hope it won't be too late.

Until then I urge my subscribers to educate yourselves regarding the supreme law of the land -- the marvelous US Constitution.

* *

Speaking of constitutionality, Clinton's attempt to shield himself from embarrassment in the Paula Jones sexual harassment case may be pointing his presidency towards a storm of constitutional controversy. The concept that some Democrats are advocating is that a sitting president is immune from the kind of lawsuit that Jones is pressing. But other experts are of the opinion that Clinton is looking for big trouble in claiming that the president is above the law. And to many critics, any claim of special presidential privilege coming from Clinton is a bit too much. Clinton has pledged over and over again to "play by the rules." Again, the Democrats from Watergate to Iran-Contra have aggressively challenged any claims to special presidential privilege.

* *

Back to taxes, I dunno, maybe the flat tax has a ghost of a chance. Malcolm Forbes in his latest *Forbes* magazine editorial came out wildly enthusiastic about a flat tax. As I noted in the last Letter, Representative Dick Armey (R-TX) has introduced a flat tax bill. Says Forbes, *"Armey's legislation would sweep away the entire income tax code, which has ballooned, over 80 years, into a multi-thousand paged monstrosity."* In the meantime, *Investor's Business Daily* (July 6) also notes the worth of Dick Armey's flat tax bill, and the paper adds that Senators David Boren and John Danforth also have a flat tax plan in the works. So does Rep. Sam Gibbons (D-FL), the new chairman of the powerful House Ways and Means committee. Russell comment: Can it happen? Will it happen? Is the flat tax an idea whose time has come? Of course it is, and if the Republicans have any brains at all they will grab the flat tax concept and push it hard. The party which can take credit for the introduction of the flat tax will, in my opinion, win the next election.

* *

Words to Ponder (from Paul Craig Roberts, former undersecretary of the Treasury): "June 13, 1994, will go down in the history of the demise of our country as the day when property lost all protection against retroactive taxation. On that Black Monday the

Supreme Court struck down the due process protection against retroactive taxation . . . Those who look to the Supreme Court to protect constitutional rights look in vain. The only way we can protect ourselves from dispossession is to carefully monitor the legislative action of those we elect." Russell comment: Clinton's retroactive income tax was an outrage. Roberts is right -- the only protection we have is to monitor how our representatives vote, and if they vote for bills like the retroactive tax bill -- oust them.

* *

The Bank Credit Analyst (located in Montreal) states that "Canada's public debt is on an explosive path . . . The recent sharp rise in Canadian bond yields and the drop in the Canadian dollar may be the start of an investor revolt against the remorseless rise in debt. It is clear that Canada's external indebtedness (net external debt equal to 170% of goods and services exports) is above the level that triggered problems in other countries . . . There are increasing signs of a taxpayer revolt, ranging from public demonstrations against municipal property taxes to outright evasion against the unpopular Goods and Services Tax. The underground economy has mushroomed." Russell comment: Canada's long-standing socialistic trend is probably coming to an end. The path of the Canadian dollar says it all. I remember, years ago, when I attended a seminar in Vancouver, the Canadian dollar was worth $1.25. The Canadian dollar is now below 72 cents, and this is in terms of the shaky US dollar. Wags now refer to Canada's dollar as "the Northern Peso." The lovely green maple leaf of Canada is turning brown.

* *

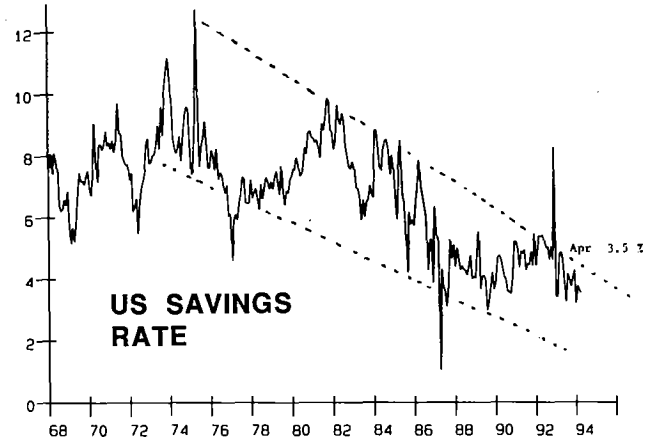
The public's interest in the Simpson trial is amazing. The LA Police Dept., the district attorney's office and the news media offices received over a thousand calls a day from amateur "who dunnit experts" during the early days of the trial.

* *

The Clinton Administration (July 6) has warned the Haiti junta to be out of there by the end of the year. The end of the year? Why stall, why give those murderers another six months? Easy, it's after the US elections.

* *

World savings rates as per Ed Hyman of *ISI*. Japan boasts a 17.3% savings rate; Germany -- 13.4%; France -- 13.5%; UK -- 10.2%; Canada -- 9.6%; **US -- 3.5%.** Chart below courtesy of *ISI*.



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No inflation? I keep getting letters like this from subscribers: "Dear Mr. Russell, we are manufacturers of tomato-based sauces. In the last two weeks we learned that: tomato paste 0.52/lb. vs. 0.47/lb. effective 7/1. Glass up 8% on 7/1. Cups up 1% on 7/1. Barrels up 6% on 7/1. From T.M., Lake Waukomis, MO."

* *

My good friend Joe Sinclair just got back from a trip to his native Iowa. Says Joe, "No wonder corn and beans have caved-in prices. I've never seen crops like I did on this trip. Corn should be knee high around now -- but it's over my head. Biggest darn crops I've ever seen. The mid-west is booming, everybody's working."

* *

If you could count one dollar bills at the rate of one a second, it would take you 31.7 years to count out a billion dollars. And at the same rate it would take you 31,699 years to count out a trillion dollars. The US federal debt is approaching five trillion dollars. Think about it.

* *

No, I am not turning this into a medical letter. Nevertheless, the July *National Geographic* contained an article on viruses that is so fascinating and informative that I want to include a few paragraphs here. "Our bodies' major defense against colds and all other virus diseases is our immune system. Extraordinarily complex, it springs into action as soon as it detects an invading virus. Every strain of virus has a uniquely shaped molecular configuration on its surface called an antigen. White blood cells known as helper-T-cells can spot these antigens and mobilize the body's defenses. Scientists have learned that tens of thousands of different contingents of helper-T-cells patrol the bloodstream, each equipped to recognize a specific antigen. This amazing diversity prepares the immune system to identify a vast array of possible invaders. Once helper-T-cells spot trouble, they alert specialized agents known as B- cells and killer-T-cells, which quickly begin to multiply. Killer-T-cells search out the cells that the virus has already invaded, chemically puncturing their membranes. Sacrificing the body's own cells, the killer-T-cells disrupt the viral takeover. B-cells produce molecules called antibodies, which bind to the invader's surface, neutralizing the virus particles.

"After the invader is destroyed, armies of long-lived T and B-cells, called memory cells, remain behind, ready to spot the virus much more quickly should it invade again. The presence of these memory cells explains why many viral afflictions, childhood diseases like measles, mumps, for instance, strike only once. After the first infection is successfully routed, the virus' subsequent invasions are quickly put down. We have become immune."

Russell comment: The problem which such diseases as influenza and HIV is that the viruses have an uncanny ability to change their makeup. Thus, the immune system is not prepared to combat the new or mutant strain. For instance, at intervals the flu virus attacks with a virulent new strain -- 1900, 1918, 1957, 1968, 1977. In 1918 20 million people died from flu, more than died during WWI. The flu virus can be carried through the air, via the wind or a cough. The one "good" fact about HIV is that it cannot live long outside the body, and is carried only through transfers of blood or body fluids. If HIV was carried through the air as is flu, we would undoubtedly have another "black death" pandemic (the Black Death or Bubonic Plague, by the way, wiped out one-third of the entire population of Europe).

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Asia's stock markets are topping out, from Hong Kong to Taiwan. China's Shanghai market index is down 75% this year, and many of China's futures markets have actually closed down. Part of the "problem" is a crackdown on inflation by the Chinese government via tight money policies.

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The US has one million people locked up in prisons, and a great many of these people are non-violent drug users or sellers. The process is getting mighty expensive, and ultimately I believe the US will have to decriminalize drugs. Why? Simple economics -- the House version of the new crime bill authorizes $13.5 billion to build more prisons, the Senate figure is half that. The cost of building US prisons is going through the roof.

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While the world and the UN watches and does nothing, the French have moved into Rwanda in an effort to halt the obvious genocide (the US administration forbids use of the word genocide). But it is genocide, and you have to take your hat off to the French. The French Foreign Legion is the main French contingent, and, of course, most of the Legion are non-French volunteers. These men are paid to fight, and they fight where their government sends them . . . Meanwhile, Clinton waivers back and forth or stalls on almost every possible foreign "decision." He's the ultimate "Public Relations President." The only trouble is that you can't run a government on popularity polls, particularly when you're not even popular.

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From Radek Sikorski in the *Asian Wall St. Journal* (May 19): "That Russia is boo ning is apparent to even the most casual

visitor. Yet Western reporting of Russia says otherwise, because Western reporting of Russia's economic transformation is fundamentally flawed. In fact, the very building blocks of most analysis of the Russian economy -- the official statistics -- vastly exaggerate Russia's woes . . . Not only is Moscow not in its death throes, the city appears to be in the midst of a boom. The number of foreign cars is growing exponentially, bright posters advertise computers and cat food, hundreds of well-stocked shops throng with customers, most of them Russian. One employee at Manhattan Express, the night-club near Red Square, where Moscow's prettiest prostitutes pick up their clients, told me that these days they charge Russians more than foreigners, because Russians are richer." Russell comment: Obviously, it all depends on what you read and who wrote it.

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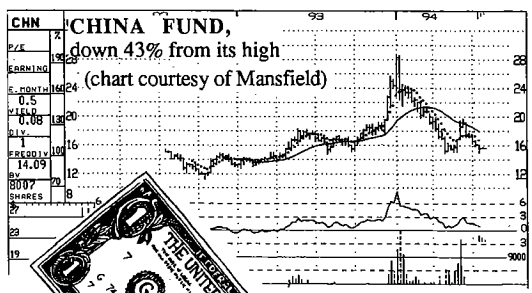
From Marc Faber's *"Gloom, Boom and Doom Report"* (2705 New World Towers, 16-18 Queen's Rd. Central, Hong Kong, Hong Kong): In view of Chinese stocks being down 60% to 75% -- "I sometimes wonder how all those great China bulls explain this situation! My explanation is simple: so far, mostly unattractive companies have been listed on China's exchanges or places overseas, while the attractive businesses (companies run by smart locals and a few foreign entrepreneurs) have not yet been permitted to raise public funds. In this respect, the Chinese government has been very smart and behaved like a true capitalist: before selling new and desirable merchandise, it got rid of the unwanted, obsolete, and old inventory to ignorant foreign buyers. Had it permitted the entrepreneurial, dynamic companies to go public, nobody would have bought the state-owned companies which were listed. So the early investors have been stuck with many rusty cans of worms."



A view on the dollar from Singapore . . .

GOLD: Let's face it, if it was easy, everybody'd be doing it. I'm talking about making money in the stock market (and we know that over any extended period of time only one out of ten ever take money out of Wall Street).

How about gold? We've been waiting and waiting and waiting for "The Big Breakout" in gold -- the decisive move over the 390 level. And over and over again gold approaches 390, only to sink back towards the mid-380s again.

Tired of guessing? Then why guess when we have what has proved to be the very reliable Gold-Primary Trend Index (G-PTI)? Study the chart. Four times the G-PTI has approached 905-910 level on the G-PTI. And each time the G-PTI has bounced off that level. Two weeks ago we witnessed the most recent attack on the 905-910 level with the G-PTI sinking to 910. But again the G-PTI held.

So we have a clearly defined three-month trading range with the G-PTI holding at 905 on the downside and the G-PTI stalling out three times in the 950-975 area.

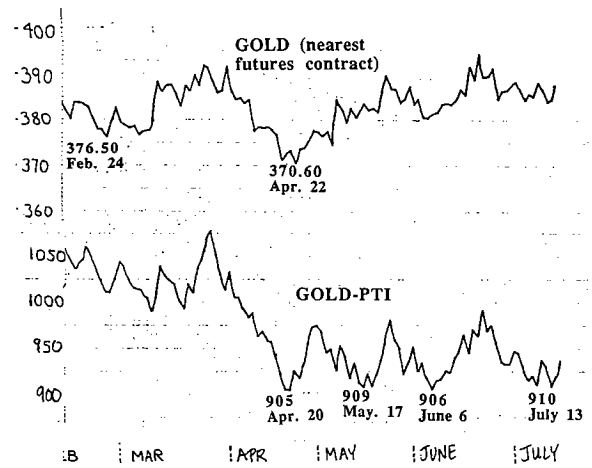
Speculators are so convinced that gold isn't going anywhere that they're selling gold options freely at 390. And selling gold calls at 400, I'm told, is tantamount to an annuity. Maybe. But this is what we need -- total skepticism regarding gold's ability to rally.

Gold-philes are particularly disappointed in gold's blah performance in the face of the swooning dollar. "What in world will make gold advance?" I'm asked. "Buyers," I reply, "lots of buyers." And that just hasn't happened yet, but I'm reasonably conviced that it will happen. But as I said earlier, if it was easy everybody'd be making money in Wall Street.

Oh yes, I know about the new anti-counterfeit dollars that will be issued shortly. Those suspecting a conspiracy (and you know who you are) are pointing to a two-tiered money system whereby our government (yours and mine) will issue two kinds of currency, one for domestic use and one to be used only overseas. Thus, if you want to take money overseas you'll have to stop at a government "kiosk" and exchange your domestic dollars for overseas dollars. Of course, they'll take careful note of the size of the exchange, your name, social security number, the amount, etc.

If this occurs I would think it would make the dollar that much less valuable. The dollar would then be a "blocked" currency, with limited use. The difference between gold (real money) and dollars (fiat currency) would also be clearly seen, since gold is accepted everywhere in any form in any quantity at any time -- this vs. a limited use "blocked" currency, literally just another a G.I. issue.

For those who are holding the actual gold or gold coins, these fluctuations and bounces around 380-390 gold doesn't mean much. But for those holding the gold stocks, it's been a "water torture" game as the stocks have slowly eroded. For those who bought the stocks early (during early 1993) this means giving back some of your profits. But for those who bought over the last six months this has been a rough ride.



NEXT MAILING: Aug. 3, 1994

LATE NOTES: On my one-point reversal Point & Figure chart gold is building an impressive bottom. But -- gold still has to break out. A spot price of 389 would be hopeful, 392 would be cause for a minor celebration, and 396 would constitute a very important upside breakout. Let's watch it. Maybe, yes, just maybe . . .

"Let the dollar seek its own level," is the Administration's policy on the buck (this is a policy?). Meanwhile, foreign interests have cut way back on their buying of US securities (can you blame them?). A big Treasury refunding coming up, and it should make for an interesting test (the test -- does anyone still want T-bonds at these yield levels?).

The D-J Averages remain in a trading range, Industrials **3593.35** on the downside, **3814.83** on the upside -- Transports **1546.02** on the downside, **1661.45** on the upside. Remember, **BOTH** Averages have to break up or down for a valid signal.